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SUBJECT: Brazil: Open Skies and Privatization Update

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1. (SBU) Summary: The president of Brazil's Agency for Civil Aviation Regulation (ANAC), Solange Paiva Vieira, outlined a detailed strategy for Open Skies negotiations with the U.S. during a March 26 meeting with Ambassador Sobel. The process involves ANAC reviewing a U.S. provided Open Skies economic impact study, hosting an Open Skies seminar that would bring together stakeholders from the private and public sectors of both countries with extensive press coverage, and finally initiating the negotiations, that, according to Vieira, would most likely involve an initial meeting of the teams (in either Brazil or the United States) to discuss objectives and expectations, followed by another session to further develop these themes. Vieira also expressed willingness to revisit the current U.S./Brazil civil aviation memorandum of understanding (MOU) in order to increase airline frequency allocations. In commenting on the GOB initiative to privatize civilian airport management through concessions, Vieira said that the deadline for the final model's submission for President Lula's review was still July 2009. She believed GOB was most likely to decide to privatize the profitable airports, in view of the need to move forward quickly on upgrades given the 2014 World Cup and Rio's bid for the 2016 Olympics. On pricing liberalization, Vieira asserted firmly ANAC's intentions to implement the initiative. End Summary.

Open Skies Roadmap

2. (SBU) Vieira stressed a pragmatic approach to Open Skies negotiations. Vieira is cognizant of strong TAM opposition to further liberalization of the Brazilian air services market, and aware that TAM has plenty of friends in Congress and elsewhere ready to support TAM's interests (see Sao Paulo septel). With that firmly in mind, Vieira clearly has a strategy to overcome domestic opposition to Open Skies and to position ANAC to be able to negotiate an agreement Congress will ratify. The first step in this process, in Vieira's view, is to build public support for Open Skies via a public diplomacy strategy. Key to launching this process, Vieira noted, is receiving the Open Skies impact study the USG has committed to provide. With that study in hand, ANAC is positioned to address accusations that Open Skies is bad economically for Brazil or somehow not to Brazilian consumers' advantage.

3. (SBU) Once ANAC has its key talking points from the Open Skies impact study, Vieira proposed the USG and ANAC work together to host a public seminar to highlight the benefits of an Open Skies Agreement between the United States and Brazil. Vieira suggested that the seminar include USG civil aviation officials, U.S. aviation economists, GOB counterparts and key stakeholders from Brazil's private sector. The seminar would be open to press and would likely take place in Rio in order to maximize positive and sympathetic press coverage. Vieira envisions the seminar focusing on the important societal benefits Open Skies creates such as operational

efficiency and lower ticket prices. The extensive press coverage would allow ANAC to build momentum toward Open Skies. In recognizing the strong opposition to Open Skies from Brazilian domestic carriers TAM and GOL, Vieira emphasized that ANAC's public relations approach will be critical to ANAC's ability to cultivate enough domestic support to be able to conclude an Open Skies agreement. She envisioned that, due to this strong opposition, an Open Skies agreement may require more than one meeting to finalize. Vieira reconfirmed that ANAC director Ronaldo Seroa Da Motta will lead the ANAC Open Skies negotiations delegation.

MOU Revisited- More Frequencies?

14. (SBU) In recognizing the fact that demand exceeded supply during the recent allocation of 2009 frequencies under the MOU, Vieira agreed she is open to a review of the MOU to increase the airline frequencies available. Specifically, Vieira offered that Rio's Galeao and Sao Paulo's Viracopos airports are capable of handling more flights, but she wasn't sure if U.S. carriers were interested in using Viracopos given its distant location from downtown Sao Paulo. Vieira commented that a review of the frequency allocations could potentially be done during the same time period as the Open Skies seminar in Rio, or sooner if wanted.

Pricing Liberalization /Privatization Schedules

15. (SBU) Vieira mentioned that ANAC will be very busy completing the proposed concession based airport management privatization model in June, in order to meet a July deadline to provide recommendations to President Lula. Vieira did not comment specifically on the

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likelihood of Rio's Galeao and Sao Paulo's Viracopos being chosen as candidates for privatization by Lula, but did indicate that GOB was likely ultimately to decide to move forward on privatizing INFRAERO's profitable airports. In addition, she asserted that all newly constructed airports will operate under this model. These comments indicate that GOB may in fact proceed with a piecemeal approach to privatization implementation versus a sector wide approach that would have grouped profitable airports with unprofitable ones (reftel B).

16. (SBU) In addressing the contentious issue of international airfare liberalization, an ANAC initiative designed to gradually eliminate the GOB's minimum pricing regime for international flights with destinations outside South America, Vieira asserted that this would be concluded soon, despite the vehement opposition from Brazil's primary domestic airlines TAM and GOL and Brazil's National Aeronautical Union (SNEA). (Note: ANAC counters TAM's and GOL's claims that neither would survive in a liberalized market environment and that both would need 10 years to effectively compete against foreign carriers, by arguing that a 30% reduction in international airfares would add an additional 2 million travelers to the current 6 million annual Brazilian international passengers, enhancing both carriers' revenues. ANAC addressed TAM and Gol's resistance by further arguing that both companies' revenues are predominately derived from domestic routes (TAM 70%, GOL 90%) and of the international routes they operate, 40% service South American destinations where pricing is already liberalized. ANAC also notes that, according to their internal studies, both companies are among the top ten most profitable airlines in the world. ANAC suffered a setback in the plan's implementation when the Brazilian Federal Appeals Court rejected ANAC's appeal of an earlier federal court decision that delayed the plan's implementation due to ANAC not having a required public audience (Note: ANAC chose to have the public audience through the internet with the intention of reaching a larger citizenry. End Note.) Besides requiring that ANAC have the public audience, the judge also suggested that this pricing plan would cause public harm and damage Brazil's economy. The lawyers for SNEA that filed the original injunction seized upon this ruling and accused ANAC of not following legally established procedures and lacking transparency. ANAC has since held the public hearing in Rio in February and is currently examining the comments received. End Note.) In commenting on ANAC's resolve to overcome these obstacles

and implement full international pricing liberalization in 2009, Vieira asserted firmly and beyond a doubt in the meeting that, "It WILL happen."

17. (SBU) Comment: ANAC has made slow, yet steady progress in its attempts to liberalize the Brazilian civil aviation sector, as seen through their most recent success in lifting operational restrictions at Rio's Santos Dumont airport despite strong opposition from Rio's governor, mayor and TAM (reftel D). Vieira's insistence that international pricing liberalization will take place and her willingness to review the MOU to open more frequencies for U.S. carriers points to ANAC's commitment to a liberalized market approach. Vieira recognizes that TAM is the primary obstacle in successfully implementing Open Skies, and the importance of winning the public relations battle with TAM will prove critical. Post believes that it is important to seize this opportunity to broaden civil aviation market liberalization, especially critical given the fact that Vieira was nominated to her position by an administration whose term will expire in 2010. End Comment.

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